and/or to sell sponsorships. The long term opportunity lies only in the ability of either the publisher or the audiotex bureau to sell sponsorships. In January 1990, Donnelley Directory tested the revenue generating capabilities of FOB sponsorships. In his test Donnelley set up 4 key objectives:

1. Determine the salability of FOB sponsorships to national advertisers;
2. Determine which applications and price points work best for different industry categories;
3. Determine the workability and cost effectiveness for Donnelley of FOB national sponsorships;
4. Determine the operational needs of supporting national sponsors.[31]

The test was considered a failure considering the number of contracts won versus the considerable effort that was expended in attempting to procure sponsorships. The national talking Yellow Pages sponsorship sales manager attributed the failure to the following:[32]

1. The audience is too small.
2. CPM is too high compared with alternative media.
3. There is no pressing need or benefit for advertisers.
4. FOB is an unproven new medium, in which no one has been able to demonstrate a link between advertising expenditures and increased sales.
5. For those advertisers interested in generating databases, the cost per name was too high.

### Building Usage

The inescapable conclusion from Donnelley's experience was its inability to generate revenue from FOB audiotex. This is linked to low usage of the product. An analysis of a 12-market FOB study (referred to as the ARC/TAG study) supports some of the suspected difficulties encountered in building usage. This study was also consistent with PBD's own experience with SMART Talk. Additionally, it was observed that reported usage might be misleading because frequent users had memorized audiotex numbers, thus eliminating the need to refer to the printed directory.

---

[31] EYP Project Manager's Memo, March 26, 1991, "Front of the Book Audiotex" (PB Document #035113-117)

[32] EYP Project Manager's Memo, March 26, 1991, "Front of the Book Audiotex" (PB Document #035113-117)

**Regulatory Environment**

Regulatory restrictions under which the PBD must operate in regard to FOB were identified as follows:

1. The appropriateness of any audiotex message in the company's directories would be out of PBD's control, and likewise,

2. The determination of who and on what terms an audiotex provider would appear in the directory would also not be within PBD's control.

The net result would be "...that PBD would lose control of the Local Access Pages section after years of investment, equity building and careful honing of the design and content."

**Conclusion**

"FOB audiotex can be of significant value to PBD if we can use it to strengthen, rather than jeopardize, our existing front-of-book editorial product. When the legal and regulatory situation permits RBOC directory publishing affiliates to shape their directory products to meet market needs, we should explore FOB audiotex."[33]

Other regulatory proceedings added to the fate of FOB at PBD. These are summarized in the following excerpts from an April 10, 1991, memo:[34]

> "Due to the ongoing proceedings at the FCC regarding the regulation of enhanced services and resulting from the Ninth Circuit Court of Appeals remand of Computer Inquiry III, the development of a front-of-book talking yellow page product would be subject to the same prohibitions PBD's electronic yellow pages development is subject to. Planning and development is currently prohibited for any enhanced service for which there is not an approved Comparably Efficient Interconnection (CEI) plan on file with the FCC. The FCC is not accepting any new CEI plans while the remand is going

---

[33]EYP Project Manager's Memo, March 26, 1991, "Front of the Book Audiotex" (PB Document #035113-117)
[34]PBD: Regulatory Issues Regarding Front-Of-Book Talking Yellow Pages, April 10, 1991, memo by S.L. Kivowitz (PB Document 035111)

on. Pending a favorable resolution of this investigation, limited market research may be conducted, but no product development activities may take place. Resolution of these issues is expected within an 8 - 12 month time frame. I will keep the product team informed of all relevant developments."

## MARKETING ISSUES AND BUSINESS PLANS

### MARKETING ISSUES

After an initial assessment of the potential for electronic services, PBD confronted the issues of how to gain entrance to the market. The primary dilemma seemed to be centered around two conflicting elements to the provision of an EYP product:

1. The value to a consumer is presumed to be the ability to take a large amount of information (a critical mass is needed) and manipulate it in the manner most personally useful - without this critical mass consumers won't buy the product;

2. On the other hand, advertisers would not likely be too interested in sponsoring a product unless there are significant volumes of usage.

By 1990, PBD had worked out a plan to deal with this dilemma. The approach involved working out a separate revenue stream to finance the development of the critical mass data base. The separate revenue stream was described as follows:[35]

> "Using the information about California business which exists currently in YPS and in Pacific Bell's list rental products, PBD would enter the list business. We would rely on the currency and depth of our information to secure competitive advantage in the existing, robust and growing business of marketing business lists to businesses seeking leads in the b-to-b marketplace. Pacific Bell is currently generating about $750,000 per year in this business with a very modest marketing and sales effort: I believe PBD could do at least as well. Bell has indicated a willingness to enter into discussions on transferring this business to PBD."

---

[35] Follow-up Memo, dated 6/6/90 "Proposed approach to EYP Market Development". (PB Document #034644 - 647)

The approach went on to describe how the marketing of business list information would allow PBD to gather and compile the kind of information needed for the creation of an EYP product. It was clearly stated that such a marketing plan would provide access to information that other methods, such as using the existing sales force, would not. Once the data base has been developed to a sufficient level, consumers would be given access to it. When the level of consumer usage reaches a sufficient level, then space could be sold to advertisers.

Internal replies and comments regarding this approach generally supported the idea. It was pointed out that the list business might be too risky to rely on to fund EYP, since it may take several years to develop into a profitable enterprise. A key strength of the approach is the lack of a heavy up-front investment. It was noted that more information should be obtained in regards to:

1. market needs,

2. identifying market needs in terms of current Yellow Page limitations, and

3. consumer and advertiser willingness to substitute electronic for print.[36]

It was also pointed out that the potential long term reward of securing a position in the marketplace was worth considerable up front risk. This is borne out by the activities of other player such as Sears, IBM, and the other telcos.[37]

**BUSINESS PLANS**

The 1992 Business Research Plan specifies PBD's intention to enter the EYP market.[38] (Appendix A) The plan focused on 4 general approaches for the year: Obtaining user feedback on product trials, database building, identifying strategic alliances, and dealing with regulatory issues. Specific activities were to include product and staff development. The first applications would be provided through the media of CD-ROM and floppy disks.

---

[36]Memo from Firoze Doctor to Hal Logan dated 6/8/90. (PB Document #034705 - 706)

[37]EYP Market Development: Response to Proposed Approach, June 12, 1990, (PB Document #035105-107)

[38]EYP 1992 BUSINESS AND RESEARCH PLAN, Document 014570 - 586

With regard to the regulatory goals specified in the plan, it was pointed out that the EYP returns could be channeled to the shareholders if the California Commission could be convinced that shareholders had borne the risk of development. It was suggested that the setting up of separate subsidiary would help ensure below-the-line treatment.

## FEASIBILITY STUDIES

In 1991, PBD contracted Haldane King and Partners to conduct EYP market feasibility studies:

> "PBD conducted this market study to aid in determining the feasibility of an EYP service. The primary objectives were to examine consumer buying information needs, map how that information is applied in the purchase process, and test preliminary assumptions about how the Yellow Pages might be electronically enhanced.
>
> The Yellow Pages is a uniquely successful sellers' medium, perceived by it s users as a convenient source of information on local businesses. California consumers report a high level of satisfaction and loyalty when asked about the Yellow Pages. Clearly, an electronic shopping information directory will need to demonstrate compelling advantages to improve on the well-understood benefits and utility of the printed Yellow Pages.
>
> As consumer markets mature and competition increases, PBD is exploring alternatives to extend the content and distribution of its buying information. These opportunities are being examined in the context of three perspectives: Consumers (business and residential), Advertisers and The Pacific Bell Yellow Pages.
>
> In order to be competitive, an EYP will have to satisfy important consumer needs, earn advertiser interest and commitment and be complementary to the existing core product.
>
> Research objectives were segmented into three primary areas:
> - Consumer Information Needs and Uses
> - Purchase Process
> - Systems and Technology"[39]

---

[39] PBD EYP MARKET FEASIBILITY STUDY FINAL REPORT , April 12, 1991 by Haldane King & Partners (PB Document #017662 - 721)

The final report of this feasibility study is in Appendix C attached to this report.

The Haldane King and Partners continued to conduct two qualitative research studies for PBD to evaluate the market feasibility of EYP[40].

## MARKET TRIALS AND RISK ASSESSMENT

### MARKET TRIALS

By 1992 PBD was planning for a market trial, as fully described in a PacBell Electronic Publishing Services (PBEPS) business plan. A comprehensive market trial was considered a very important step toward starting up an electronic publishing business, since it was necessary to be able to predict the viability of the proposed business by testing usage and participation. At the same time PBEPS would be able to test its ability to create and deliver a database over a variety of media. With such information a full business case could then be developed. The plan was to conduct the market trial during 1993 and present a business case in 1994.

This first market trial would utilize live operators as an interface between the user and the database, and would focus on some basic services such as access to the basic yellow page listing and business listing tiers. The addition of hours of operation would be an important selling point. Most inquiries would be via a live operator (provided by a 3rd party vendor) but other options will be tested. It was anticipated that these other options would include providing the answer to inquiries via:

- computer-generated voice,
- voice mailbox,
- mailed printout,
- fax, and
- computer to computer.

Advertising the market trial was to be a test in itself as to whether one media works better than another in marketing this product. TV, print, radio, billboards and promotions were all to be utilized.

[40]PBD ELECTRONIC YELLOW PAGES, "Classified Advertising Research Study Proposal", February 3, 1992 Prepared by Haldane King & Partners. (PB Document #032534)

Joint venture was a prominent topic in the discussions concerning the market trial plan. In fact Pacific Bell's Information Services was an active joint venture candidate. PBEPS' roll in any joint venture trial was clearly stated: "PBEPS will be the database provider for these trials."[41]

**RISK ANALYSIS**

The various anticipated risks were laid out in the business plan in three categories:

- Marketplace and Business Structure Risks,
- Technology Risks, and
- Legal and Regulatory Risks.

It was anticipated that the structural risk would involve the upfront cost of providing a product close enough to being final as necessary to attract users and advertisers. Most of this would be related to setting up the market trial, and would include the associated advertising expense necessary to ensure that sufficient promotion has been utilized. The Marketplace strategic risks were identified as those parameters that the market trial would be designed to test.

Technology risks lie in the fact that the media of the future is largely an unknown, and such a product needs to be flexible enough to deal with this unknown.

In the view of the company in 1992, [

REDACTED

] Risk issues relating to regulation by the California Public Utilities Commission were identified as follows:

[THESE BULLETS HAVE BEEN REDACTED ☞☞

---

[41] Pacific Bell Electronic Publishing Services Co.'s Database and Consumer Products Projects, Preliminary Funding Request, August 4, 1992 (PB Document #014552 - 568)

REDACTED]

"In insisting that ratepayers not be disadvantaged by the disclosure of intellectual property to a below-the-line subsidiary, the Commission noted that 'Ratepayers may be disadvantaged if the intellectual property is used by the competitive affiliate to provide a service which could have been provided at lower cost by the monopoly, but for corporate reasons, the company decided against the deployment of the service in a regulated setting.'[42]

ALTERNATE ENTRY OPTIONS

[

REDACTED

]other options were also considered but considered less desirable for various reasons.

[.

REDACTED

]

The above options were rejected as less desirable for different reasons. Either the market had been found wanting ([ REDACTED ]), or there was a lack of competitive advantage at this time ([ ).

REDACTED

].

---

[42]Ibid.

[

REDACTED

] Pacific Bell's Information Services Group and Corporate Strategy department examined this option carefully several years ago, and found it wanting. There is no reason to believe that a re-examination now would lead to a different conclusion.

## PBD'S EYP IS AN "EXTENSION OF PRINTED YELLOW PAGES"

It was difficult for the Audit Team to trace all the documents and analyze and draw a conclusion on what exactly transpired through the many years of EYP development of PBD. However, from those documents obtained by the NARUC Audit Team, one fact is undeniable: Even today's EYP database design bears a startling resemblance of what was conceptualized in 1988. In fact, the whole product EYP was built from the idea of enhancing existing printed yellow pages.

In the Pacific Bell Information Services 1992 Business Plan Overlay, dated August 21, 1991, PBD recognized that:

> "Pacific Bell has many possible opportunities within the Information Services Industry, with varying degrees of attractiveness..
> Some of these opportunities are extensions of current products or product lines..EYP"
>
> "In addition, some have synergies with existing products or other information services products:
> ...[
>
> REDACTED
>
> "...The top opportunities have been selected, based on the market attractiveness, fit with Pacific Bell and capabilities developed inherent with the product:
> ...[
>
> "[43] (emphasis added)

[43] Pacific Bell Information Services 1992 Business Plan Overlay, dated August 21, 1991 (PB Document #034887 - 923)

Thus, the EYP was built and reportedly continued to be built as it expands to the frontier of the multi-media publishing arenas. Although Pacific Bell parent corporation may want to transfer EYP out of the operating company and EYP may eventually be developed into a multi-media publishing group of services, one thing is clear: EYP's origin cannot be denied. This EYP, or EPS product, is an extension of the old printed yellow pages.

## SUMMARY

As best as can be determined, the ratepayers' funding of the these potential new electronic publishing services and products began in the mid-1980s, a period of over eight years. A major impetus to this electronic publishing effort began when a key outside expert in the field of electronic publishing was hired by Pacific Bell Directory to lead the effort. The visionary strategy and direction of electronic publishing was provided by the former President of Pacific Bell Directory Company.

Substantial amount of staff resources at Pacific Bell Directory were involved in the research and development of potential electronic publishing services and products. Numerous feasibility studies were made by outside consultants and by Pacific Bell Directory's own experts regarding the market potential for electronic yellow page publishing and other related line of businesses.

These studies generally show that the market potentials for the offering of electronic yellow publishing services and products by a RBOC are favorable. The RBOCs are in a favorable competitive position in the emerging electronic yellow publishing because of the synergy from the companies' core telephone operations, namely, name recognition, established reputation, expertise in classified advertising, customer contacts and relationships, infrastructure, facilities, etc.

# CHAPTER 7

## CORPORATE PLACEMENT OF EYP

### PACIFIC BELL CHOSE TO DEVELOP EYP WITH RATEPAYER FUNDS

The development of EYP opens a page of extensive research efforts drawing huge man-hours and many consultants in a span of many years. While the new product is a natural extension in an enhanced fashion that fits rightly with PBD, the cost of development was also borne by ratepayers from the project conception. Pacific Bell could have, however, designated the funding and development to be carried by an unregulated "below-the-line" affiliate, without any linkage or coverage from PBD, from the project conception, as it would have been appropriate, logical and consistent with its current application with the California Commission. Instead, Pacific chose to have ratepayers fund the early development of EYP and years later, transfer the responsibility to an essentially non-regulated entity.

As early as 1987, corporate placement of the new business opportunity was apparently on the mind of the then CEO, Mr. John Gaulding. Gaulding assumed that some form of *sharing* would result from the Rate Stabilization proceeding before the California Commission, and that the growth and earning power of PBD would make the Company a strong candidate for investment in areas such as EYP, that was not strictly traditional:[44]

### PBD'S FUNDING TRACK

In a memo to the EYP Project Manager, dated September 20, 1990, while claiming that a PC-based model of an on-line EYP product had been developed for purposes of product concept illustration and ready for demonstration:

> "Incremental funding has been allocated to the project in the following amounts, primarily to conduct consumer market demand analysis:
>
> 1990: $250k
> 1991: $400k

[44]"A BLUE PRINT FOR THE FUTURE", PBD Presentation to the Board of Directors, September 24, 1987 (Document #021545 - 021581)

An integral PBD Task Force has been formed to develop PBD's strategic perspective on EYP; the Task Force is represented by the following PBD functional departments: Business Development, Core Product Marketing, Information Systems, Public Policy, and Finance.

The PBD EYP Task Force is maintaining relations with Pacific Telesis Corporate Strategy and Pacific Bell ISG."[45]

It was reported in the EYP Progress Report, dated June 22, 1990, that PBD, PB/Information Service Group and PB/Planning had begun to assess the elements of the regulatory situation:

- Optimal placement of EYP development within the Telesis family
- Will the California Commission place EYP above or below the line?
- Should EYP be developed within a regulated or deregulated framework?

The EYP Progress Report also cited that:

- EYP has important revenue and profit potential for PBD
- PBD database provides a potential competitive advantage

Nevertheless, the EYP Progress Report concluded that the recommended EYP development strategy would need to be pursued with funding from Pacific Bell. It reminded that formal designation of PBD as the Pacific Telesis Company with primary responsibility for the development of EYP should accompany Pacific Bell funding.[46]

In 1991, the 1992 PBIS Business Plan proposed that:

"An information Services Growth Fund should be established within Pacific Bell to finance new Information Services opportunities in 1992.

Funds should be allocated to opportunities based on Pacific Bell's appetite for new, potentially risky, but growth opportunities in 1992, and on individual opportunities' strategic fit with Pacific Bell, and financial and market attractiveness.

---

[45] Memo to the EYP Project Manager, dated September 20, 1990 (PB Document #034695 - 696)

[46] EYP Progress Report, June 22, 1990 (PB Document 034588 - 623)

Additionally, Pacific Bell should develop methods to allow the network to be the conduit for other Information Services providers, acting as the platform upon which Information Services applications can be built."[47]

It is an undeniable fact that the EYP was developed by PBD using funds from ratepayers. Nevertheless, the hands of the Telesis Corporate intervention were written all over the wall even in the very early days.

## TELESIS PLACEMENT DECISION OF EYP

When the new director of the New Business Development was hired in 1988, he was instructed to engage in research to answer the quest of the EYP vision of former CEO, John Gaulding. At the same time, he was also reporting directly to Phil Quiqley, the then CEO of Pacific Bell. By 1991, the EYP Task Team was instructed:

"Obviously, any application we pursue will require regulatory approval. One potential wrinkle: Quigley has stated that any electronic product offering will be below the line; this may complicate some of PBD's plans."[48]

In 1992, the question of managing effectively the simultaneous offering of Yellow Pages data in print by one organization within Pacific Telesis Group, and of similar data in electronic form by another organization within the company was raised.[49]

### TELESIS JUGGLING OF EYP PLACEMENT

In 1991, the Pacific Bell Electronic Publishing Services (PBEPS) was formed. Pacific Bell informed the Audit Team that PBEPS was never active and was dissolved later. On January 1, 1993, the Project Manager of EYP was transferred to PBIS. Along with this transfer, the IMS manager who was involved in designing the EYP database was also transferred. On April 1, 1994, Pacific Bell announced that the entire EYP Team was transferred to a new Pacific Telesis Electronic Publishing Services that was not part of Pacific Bell. It appears that this formation was a step to shield the potential lucrative business from regulation.

---

[47] Pacific Bell Information Services 1992 Business Plan Overlay, August 21, 1991 (PB Document #034887 -993)
[48] EYP Meeting Notes, May 10, 1991 (PB Document #034876)
[49] YPD Business Case Summary, Preliminary Funding Request (Document #016467)

## SUMMARY

In designating the EYP to below-the-line non-regulated affiliate, ratepayers are being denied of the future benefits from an asset they funded.

The change in Pacific Bell corporate strategy to that of prohibiting Pacific Bell Directory from engaging in research and development, or from offering of electronic delivery or enhancement of the core yellow page information business have left the company with a mature business with a declining growth rate. This strategy has removed from Pacific Bell Directory a potential new source of revenues to offset the potential loss of classified yellow page advertising revenues to emerging electronic publishing competitors and potentially to its newly formed affiliate company, the latter, being a form of cannibalization.

The Pacific Telesis Group's strategy, if unchanged, has left a billion dollar regulatory ratemaking asset without the means to enhance in a significant way or even to maintain its industry position over the long-term. This change in Pacific Telesis' corporate strategy appears to have been made to ensure that only the shareholders benefit from the activities funded by the general body of ratepayers.

# CHAPTER 8

# OTHER ISSUES AND PROBLEMS

In the course of the investigation, the NARUC Audit Team discovered many other issues and problems concerning EYP. All of them are significant issues that require correction or resolution:

## IMPROPER PROJECT ACCOUNTING AND TRACKING

In Pacific Bell's application to the California Public Utilities Commission for permission to enter electronic publishing, Pacific only reported $1.5 million as an accumulated expenditure. However, according to the project director of EYP, accounting and tracking of the EYP expenditure was not done at all and there was "no tracking manual". He admitted that tracking began only after meeting with the Audit Team in the last quarter of 1992.[50]

## AFFILIATE TRANSACTION RULES MAY NOT BE ADEQUATE

There have been no compensation for ratepayers' multi-million dollar risk. Pacific Telesis' electronic publishing ventures have been cross-subsidized by ratepayers. Current affiliate transaction rules may not be adequate to prevent or deter similar situation from occurring. A situation where ratepayers, in essence provide the seed money and bear the risks with the rewards accruing to shareholders.

## MAJOR INVESTMENT IN NEW INFORMATION MANAGEMENT SYSTEM INCAPABLE OF HANDLING THE EYP DATABASE

PBD informed the Audit Team that the major investment in its new Information Management System (IMS) is incapable of handling the EYP database. This statement is contrary to the company's own documents and studies and PBD management presentation which uses IMS flexibility in delivering new products requirement as a selling point to the Board of Directors to replace the old data system. IMS was designed and installed at the same time when EYP was developed.

---

[50]Meeting with Hal Logan, EYP Project Director, February 23, 1993

## OTHER CRITICAL ISSUES

This report reveals the development of EYP by PBD, the various development stages and roadblocks PBD faced, the analyses of the opportunity and risks EYP brings along, and the Corporate involvement in the soon-to-be-realized business. Nevertheless, many concerns and issues are still open: the cannibalization of EYP on printed yellow pages, the protection of existing printed yellow pages contribution for ratepayers, the competition issues, the regulatory policy concerning the two yellow pages forms, the balancing of risk and reward, the right of the ratepayers' funding, the future scenarios of EYP as it expands its horizon to electronic publishing and the placement of the service above-or below-the-line.

# CHAPTER 9

## FINDINGS AND CONCLUSIONS

No prudent company would enter into a new business venture without careful and extensive studies concerning the nature of the new business, its market, its prospective customers, requirements of various kinds, such as financial, legal, and regulatory, and measurement of business risks. The development of Electronic Yellow Pages is no exception.

Pacific Bell Directory's development of Electronic Yellow Pages can be traced back to 1986, some eight years ago. Because of the long span of time and the complexities of the new product, the NARUC audit has been difficult. This NARUC Audit Report serves to provide an insight of how the Electronic Yellow Pages came into being, what issues and concerns Electronic Yellow Pages brings, and how the Telesis corporate decision juggles the placement of Electronic Yellow Pages out of Pacific Bell, the telephone operating company.

The following is a list of the Audit Team findings and conclusions:

1. The yellow page operations of Pacific Bell Directory, a wholly owned subsidiary of Pacific Bell, are considered to be part of the regulated rate base in California. All revenues and expenses associated with yellow page operations are thus considered "above-the-line" for ratemaking purposes, unless specifically excluded. This regulatory treatment started early in the corporate history of Pacific Bell (then known as Pacific Telephone and Telegraph Company) and continues to the present. All of the substantial contribution from the yellow page revenue streams is used to offset the cost of exchange operations.

2. Pacific Bell Directory's research and development and associated activities in electronic publishing and other emerging technology in the directory field were funded by the general body of ratepayers.

3. As best as can be determined, the ratepayers' funding of the these potential new electronic publishing services and products began in the mid-1980s, a period of over eight years.

4. A major impetus to this electronic publishing effort began when a key outside expert in the field of electronic publishing was hired by Pacific Bell Directory to lead the effort. The visionary strategy and direction of electronic

publishing was provided by the former President of Pacific Bell Directory Company.

5. Substantial amount of staff resources at Pacific Bell Directory were involved in the research and development of potential electronic publishing services and products.

6. Numerous feasibility studies were made by outside consultants and by Pacific Bell Directory's own experts regarding the market potential for electronic yellow page publishing and other related line of businesses.

7. These studies generally show that the market potentials for the offering of electronic yellow publishing services and products by a RBOC are favorable.

8. The RBOCs are in a favorable competitive position in the emerging electronic yellow publishing because of the synergy from the companies' core telephone operations, namely, name recognition, established reputation, expertise in classified advertising, customer contacts and relationships, infrastructure, facilities, etc.

9. Over the mid- to long-term, electronic publishing will offer serious competition to the traditional printed yellow pages. Unmitigated, substantial erosion of the present contribution from traditional printed yellow pages in the order of magnitude of millions of dollars will occur for Pacific Bell ratepayers.

10. All research and development activities were abruptly discontinued (about January 1993) at the Pacific Bell Directory. Key personnel and the electronic publishing activities were transferred to an essentially non-regulated subsidiary, Pacific Bell Information Services, a wholly owned subsidiary of Pacific Bell.

11. After about a year, a further transfer was made of this electronic publishing operation to a newly formed company that is not part of the Pacific Bell corporate structure, but is part of Pacific Telesis, the holding company.

12. The change in Pacific Bell corporate strategy to that of prohibiting Pacific Bell Directory from engaging in research and development, or from the offering of electronic delivery or enhancement of the core yellow page information business has left the company with a mature business with a declining growth rate.

13. This strategy has removed from Pacific Bell Directory a potential new source of revenues to offset the potential loss of classified yellow page advertising revenues to emerging electronic publishing competitors and potentially to its newly formed affiliate company, the latter, being a form of cannibalization.

14. The Pacific Telesis Group's strategy, if unchanged, has left a billion dollar regulatory ratemaking asset without the means to enhance in a significant way or even to maintain its industry position over the long-term.

15. This change in Pacific Telesis' corporate strategy appears to have been made to ensure that only the shareholders benefit from the activities funded by the general body of ratepayers.

16. Pacific Bell Directory's accounting and project tracking guidelines and procedures are inadequate with respect to the electronic yellow pages development project. This project and related electronic publishing projects are controversial from a regulatory perspective, especially in view of the fact the research and development efforts started before the lifting of the information ban. The company did not start tracking its expenditures until the fourth quarter of 1992, approximately six years after the work began. Moreover, this tracking began only after this issue was raised by the Audit Team.

17. There have been no compensation for ratepayers' multi-million dollar risk. Pacific Telesis' electronic publishing ventures have been cross-subsidized by ratepayers.

18. Current affiliate transaction rules may not be adequate to prevent or deter similar situation from occurring. A situation where ratepayers, in essence provide the seed money and bear the risks with the rewards accruing to shareholders.

19. There is presently a proceeding pending before the California Public Utilities Commission in Application No. 93-11-031, dated November 12, 1993, in the matter of the Application of Pacific Bell and Pacific Bell Information Services to notify the Commission to enter Electronic Publishing Service Market, where some of the issues identified in this report are expected to be addressed. Hearings for this proceeding have been scheduled in August 1994.

# APPENDICES

# PART

# C

# APPENDIX A

# Pacific Bell
# Electronic Yellow Pages

## Vision and Development Strategy

### The vision and plan to collect, manage and publish enhanced "Yellow Pages" information services to California customers.

Hal Logan
Director, Business Development
Pacific Bell Directory

November 1991

# APPENDIX A

THIS IS A NINE PAGE DOCUMENT COVERING EXCERPTS FROM PACIFIC BELL ELECTRONIC YELLOW PAGES VISION AND DEVELOPMENT STRATEGY, CONSULTANTS' ANALYSES AND REPORTS. THE MATERIAL IN THIS DOCUMENT IS CONSIDERED PROPRIETARY BY PACIFIC TELESIS GROUP AND HAS BEEN REDACTED.

# APPENDIX B

# Pacific Bell Directory
# EYP Product Overview

# Electronic Smart Pages
# (ESP)

October 8, 1991

Prepared by:

Thomas Morgan
InterMedia Development Corporation

Prepared for:

Hal Logan
Director, Business Development
Pacific Bell Directory